TRANSCRIPT

FEDERAL OPEN MARKET COMMITTEE CONFERENCE CALL

December 12, 1980

Prefatory Note

This transcript has been produced from the original raw transcript in the FOMC Secretariat's files. The Secretariat has lightly edited the original to facilitate the reader's understanding. Where one or more words were missed or garbled in the transcription, the notation "unintelligible" has been inserted. In some instances, words have been added in brackets to complete a speaker's thought or to correct an obvious transcription error or misstatement.

Errors undoubtedly remain. The raw transcript was not fully edited for accuracy at the time it was produced because it was intended only as an aid to the Secretariat in preparing the record of the Committee's policy actions. The edited transcript has not been reviewed by present or past members of the Committee.

Aside from the editing to facilitate the reader's understanding, the only deletions involve a very small amount of confidential information regarding foreign central banks, businesses, and persons that are identified or identifiable. Deleted passages are indicated by gaps in the text. All information deleted in this manner is exempt from disclosure under applicable provisions of the Freedom of Information Act.

Meeting of the Federal Open Market Committee

December 12, 1980

A meeting of the Federal Open Market Committee was held on Friday, December 12, 1980, at 12:40 p.m., at the call of Chairman Volcker. This was a telephone conference meeting, and each individual was in Washington, D. C., except as otherwise indicated in parentheses in the following list of those participating.

PRESENT:

Mr. Volcker, Chairman	
Mr. Solomon, Vice Chairman	(New York)
Mr. Gramley	
Mr. Guffey	(Kansas City)
Mr. Morris	(Boston)
Mr. Partee	
Mr. Rice	
Mr. Roos	(St. Louis)
Mr. Schultz	(Atlanta)
Mrs. Teeters	
Mr. Winn	(Cleveland)

Messrs. Balles (San Francisco), Baughman (Dallas), and Mayo (Chicago), Alternate Members of the Federal Open Market Committee

Messrs. Black (Richmond), Corrigan, and Ford (Atlanta), Presidents of the Federal Reserve Banks of Richmond, Minneapolis, and Atlanta, respectively

Mr. Altmann, Secretary
Mr. Bernard, Assistant Secretary
Mr. Petersen, General Counsel
Mr. Oltman (New York), Deputy General Counsel
Mr. Holmes (New York), Adviser for Market Operations
Mr. Axilrod, Economist

Messrs. J. Davis (Cleveland), T. Davis (Kansas City), Ettin, Henry, Keir, Kichline, Truman, and Zeisel, Associate Economists

Mr. Pardee (New York), Manager for Foreign Operations, System Open Market Account

Mr. Sternlight (New York), Manager for Domestic Operations, System Open Market Account

Mr. Allison, Secretary, Office of the Secretary, Board of Governors
Mr. Coyne, Assistant to the Board of Governors
Mr. Prell, Associate Director, Division of Research and Statistics, Board of Governors
Mr. Beck, Senior Economist, Banking Section, Division of Research and Statistics, Board of Governors
Mrs. Deck, Staff Assistant, Open Market Secretariat, Board of Governors

Messrs. McIntosh (Boston), and Smoot (Philadelphia), First Vice Presidents, Federal Reserve Banks of Boston and Philadelphia, respectively

Messrs. Boehne (Philadelphia), Brandt (Atlanta), Burns, (Dallas), Danforth (Minneapolis), Fousek (New York), Keran (San Francisco), Parthemos (Richmond), and Scheld, Senior Vice Presidents, Federal Reserve Banks of Philadelphia, Atlanta, Dallas, Minneapolis, New York, San Francisco, Richmond, and Chicago, respectively

Mrs. Nichols (Chicago), Vice President, Federal Reserve Bank of Chicago

Mr. Burger (St. Louis), Assistant Vice President, Federal Reserve Bank of St. Louis

Mr. Campbell (New York), Assistant Secretary, Federal Reserve Bank of New York

Transcript of Federal Open Market Committee Conference Call of December 12, 1980

CHAIRMAN VOLCKER. Why don't you bring us up to date, Mr. Axilrod.

MR. AXILROD. Thank you, Mr. Chairman. Since last week the data we've gotten on the aggregates appear to be somewhat weaker on balance. We will be publishing today levels of M-1A and M-1B that will essentially show very little change from the revised levels for the week of [November] 26th. The partial data that we have for the week of [December] 10th again suggest very little change from the levels of the 3rd. So, since mid-November we've had about four weeks of an unchanged money supply.

CHAIRMAN VOLCKER. And you have a downward revision for last week.

MR. AXILROD. For the week of the 26th we will revise down [the preliminary figure] we have already published.

MR. GRAMLEY. What are the numbers for the 26th and the 3rd, Steve?

MR. AXILROD. Governor Gramley asked for the numbers for the 26th and the 3rd. For M-1A they are: $388.9 billion for the 26th; $388.7 billion for the 3rd; and [based on] a partial estimate $388.6 billion for the 10th. The pattern of M-1B is essentially the same, slightly higher.

CHAIRMAN VOLCKER. And the published figure for the 26th was what?

MR. AXILROD. The published figure for the 26th had been $389.6 billion and we will revise that to $388.9 billion. With these figures coming in, we have weakened our estimate of growth in M-1A for December to 2-1/2 percent from the 3.7 percent we had last week. [Growth of] M-1B remains just under 5 percent. We also have weaker data coming in on small time deposits and our estimate of M2 growth for December, which last week was 6 percent, has been reduced to 5 percent, reflecting essentially this weakening in small time deposits.

CHAIRMAN VOLCKER. What are the November figures?

MR. AXILROD. For M2 growth the revised figure for November is an 11 percent increase.

CHAIRMAN VOLCKER. For M-1A and B?

MR. AXILROD. For M-1A the November figure, slightly revised, is 7.1 percent and for M-1B it's 9.3 percent. But this weakening in the recent numbers, Mr. Chairman, tends to weaken required reserves very slightly. And we ended up last week coming in very close on the borrowing; it was $1,786 million at the end of last week. Taking that into account and the previous weeks, and the weakening of required reserves, we would tend to have a somewhat lower level of borrowing implied from our reserve paths in the weeks of [December] 17th and 24th. There is some uncertainty about that level of borrowing, which might be anywhere between, say, $1.6 billion and a little over $1.7 billion. It depends in part on technical adjustments that could be made to the multiplier; there is some remaining doubt about that.

Two other points I would add, Mr. Chairman. One is that the gap between total projected reserves, which reflects the actual behavior of money, and the total reserve path set in the light of the Committee's decision at the November meeting had been quite wide at the beginning of the period and is narrowing. Total reserves are now projected at roughly $200 million above the path. And they had been orders higher at earlier periods. The other thing, Mr. Chairman, if it is of interest to the Committee, is that based on the data we now have M-1A growth for the year measured from Q4 '79 to Q4 '80 looks as if it will be 5-1/2 percent. M-1B growth looks as if it will be 7-1/2 percent, and M2 growth will be about 9.8 percent. In the case of M-1A, that's just below the upper end of the range. M-1B is just above the upper end and M2 is about 0.8 above the upper end of its range.

CHAIRMAN VOLCKER. I think it would be correct [to say] with those M-1A and M-1B ranges that they would both be about 1/2 percent above for the year.

MR. AXILROD. Well, yes, if we adjusted for the fact that when the ranges were originally set M-1B was set to grow 1/2 point more than M-1A. In the event, there were a lot more shifts out of demand deposits and other assets into ATS accounts than we had expected, [largely as a] consequence, I think, of the Monetary Control Act and banks wanting to get into the business fast before thrifts get into the act this coming year. If we adjusted for that, then of course we would want to lower the M-1A range and raise the M-1B range. I think the outcome would be just about as you described it.

CHAIRMAN VOLCKER. On the international batting average, that probably puts us at the top.

SPEAKER(?). Right.

CHAIRMAN VOLCKER. Mr. Sternlight, do you want to add anything about the market?

MR. STERNLIGHT. Well, the markets have had a pretty turbulent period. The money market rates have been shooting up very sharply in the last several days. Some of the rates are steady today because they have been pushing up, especially for [unintelligible] and commercial paper. But they are steady, of course, at a very high level. In some other sectors, [such as] the Treasury bill market and the Treasury coupon market, there has been some recovery in prices--declining rates--today, making up a modest part of the erosion of recent days. The federal funds rate averaged 18.80 percent in the last statement week. Funds were trading at about 20 percent yesterday; the rate is around 19-1/2 percent today. It is very, very hard to say where things might settle down with this range of borrowing that Steve mentioned of $1.6 to $1.7 billion. I would expect the funds rate could stay in that 19 to 20 percent range for a little while, although perhaps after things settle down more that degree of borrowing might be consistent with a funds rate a shade lower than I mentioned.

CHAIRMAN VOLCKER. Mr. Truman, do you want to review international markets briefly? Or Mr. Pardee can do it. I'm sorry, I forgot [you were here since we're] on the telephone. Out of sight, out of mind. Mr. Pardee.

MR. PARDEE. The exchange markets have all been going rather well, and in the last couple of days the dollar has continued to rise. Today we are in a situation where the [unintelligible] was probably nearly a 2 percent range. The dollar has moved above the 2 level against the Deutschemark. It got as high as 2.03-1/4 this morning. Again, it [unintelligible] interest rate. The situation in Poland has been a matter of continuing concern. And that brought [unintelligible] for the background in the last few days. We are hearing, however, that a number of U.S. corporations, instead of selling [foreign] currencies to buy dollars for their year-end [repatriation] of funds, are borrowing dollars in the Euromarket and using that as a mechanism to bring funds home. This [reflects] the expectation that the exchange rate won't be so high for the dollar after the year-end. But they are adding pressure to these Eurodollar markets; in one month the Eurodollar rate went as high as 24 percent--that was this morning in the early hours. We have [unintelligible] a big flow out of the Middle East. Neither [unintelligible] in the last couple of days are the expectations that the rate will turn around. We buy marks, [scaling] back our operations a bit now that the Treasury is covered on the Carter notes. And we are almost fully [up to our limit]; we have about $1.45 billion worth of marks under our authorization of $1-1/2 billion. They were sitting quietly on the day. Of the marks we are taking on now [most] we have put on to the Treasury.

CHAIRMAN VOLCKER. I would only add, as was implied by some of these other comments, that I think it goes beyond that. There is somewhat of a "fin de guerre" developing in some markets, reflected in part in commodity markets. We have such a strong and stable system of financing commodities and commodity speculation now that when the price declines and retraces in a week the price increase of the previous three months, people wonder whether [investors] can meet margin calls. And they are substantial. All sorts of rumors--unwarranted rumors I trust--began floating around those markets yesterday. The gold market, as you know, is down substantially in the face of the Polish news and continuing unrest in the Middle East and all the rest--factors that we ordinarily think would raise the gold price. And commodity markets are down basically by limit amounts in successive days across the board. I think it's also fair to say with all this [churning] in the money market, that the banks are beginning to get a little worried. I don't think a bank is [unintelligible] alone for months. They are all beginning to wonder where they are. This movement in the CD market reflects a rather sudden concern as to whether they really can fund themselves and they want to take out a little insurance. But the market rates have a certain life of their own at this point--or did up to this morning anyway--reflecting psychology rather than the normal relationships that one would expect between borrowings and federal funds rates and other rates. There is a lot of talk about the prime rate at the moment. Of course, with this rapid movement in short-term rates, it is below its normal relationship with market rates by a significant amount. I don't know whether the banks will [hold] off on changes for a while, pending some feeling [that things will] settle down, or whether they will be impelled by their current fears to move rather earlier and by sizable amounts. I just don't know. I don't know whether anybody else has any comment on the developing situation.

MR. MAYO. Paul, Bob Mayo [in Chicago]. I think I should add, just on the commodity market, that the Board of Trade did open this morning and went down its limit but has recovered somewhat since, in what I imagine would be the [unintelligible] in financing of those accounts. They felt reasonably comfortable as of 11 o'clock this morning, with perhaps one exception, that things aren't going to blow up on them. The president of the Board of Trade is in the process of putting out a statement this morning. Our people are over there watching to see what is going on and we have our fingers crossed that things don't seem to be continuing to [reflect] all the excitement that the rumors produced yesterday afternoon.

CHAIRMAN VOLCKER. Right. Anybody else have any comments? Well, my proposal under the circumstances will be very simple. We are meeting next week. And we took an interim flexibility action. I would propose that we act with discretion during this period, try to meet our reserve objectives but balance operations a little in terms of what is going on in the market at the moment, without putting any formal limit on the federal funds rate. That seems to me to continue to be appropriate until we see how this market develops in the next week. I say that because I don't like to put a precise limit on the federal funds rate in these circumstances because on particular days it can obviously move in an exaggerated way. On the other hand, I think we need a little leeway from necessarily following a fully mechanical target under these conditions if the more frantic developments did seem to be breaking out in this market. Last week we successfully accomplished this without deviating much from what would have been normal practice. In fact, we came out within $30 million or something like that of the borrowing target. We came out with a higher federal funds rate, I suppose, than would have been anticipated, but not all that much higher. We were not guided by a precise limit on the rate, and I think that was helpful. So that would be my proposal--just to carry over for another week until we meet again on Thursday afternoon.

MR. PARTEE. Chuck Partee. That's fine with me.

SPEAKER(?). It's fine with me, too.

MR. BALLES. John Balles. That sounds good to me.

SPEAKER(?). I would buy that, too, this morning.

SPEAKER(?). Okay.

MR. ROOS. Roos. Okay.

MR. GUFFEY. Guffey. Okay.

MR. BAUGHMAN. Dallas. Okay.

MR. WINN. Winn. Okay.

MR. FORD. Atlanta is with you.

MR. BLACK. Same in Richmond.

VICE CHAIRMAN SOLOMON. New York. Okay. I assume that will be in the official records, Paul.

CHAIRMAN VOLCKER. Yes, I think we will record that at this meeting we just extended the authority given last week.

SPEAKER(?). Until the next meeting.

CHAIRMAN VOLCKER. Until the next meeting--or until the directive is changed, presumably. Do I assume we have [a consensus]? Oh, wait a minute, we [haven't heard from] the people here at the table.

SPEAKER(?). Yes, it's all right with me.

SPEAKER(?). Okay.

CHAIRMAN VOLCKER. Governor Teeters wants a low limit on the federal funds rate, I guess. So we're 11 to 1, I think, without having to call the roll again.

MR. ALTMANN. 10 to 1.

CHAIRMAN VOLCKER. 10 to 1? Who's missing?

MR. ALTMANN. Henry is missing.

CHAIRMAN VOLCKER. Oh yes, Governor Wallich is missing. That's right. [We're through] unless someone has something else to say. I might mention, as I am sure is clear to all of you just from reading the newspapers, that the retail sales figures came in strong. We also have some figures, so far as the survey is concerned--I don't know what the reality is--that show a stronger outlook for plant and equipment spending in the early part of next year. If we take the retail sales figures at face value, I suppose it solves part of the mystery of why production seems to be rising faster than sales while everybody reports not much inventory [overhang]. We will go over this in considerable detail at the meeting, I am sure, but I understand that under the circumstances GNP is expected to be higher in the fourth quarter than previous projections indicated. Is that a fair comment, Mr. Kichline?

MR. KICHLINE. Yes it is.

MR. PARTEE. How much of an increase do you have now?

MR. KICHLINE. We have an estimate for real GNP growth of 4-1/2 percent at an annual rate in the fourth quarter.

MR. PARTEE. How much price?

MR. KICHLINE. Well--

MR. PARTEE. What's the nominal?

SPEAKER(?). It must be about 17 percent because they had borrowed--

MR. KICHLINE. About 18 percent.

MR. PARTEE. 18 percent nominal?

MR. KICHLINE. Right.

MR. PARTEE. Well that explains quite a bit.

CHAIRMAN VOLCKER. I think it explains quite a bit about the pressure on the money market and the money supply. I might say just for the record that the money supply estimate Steve gave you for December is based, obviously, upon projections for the second half of December. I personally attach very little weight to it at this point. It could be higher or lower. They do assume an increase in the second half of December rather than a decline or this evenness.

MR. AXILROD. Mr. Chairman, if I may just correct that a bit, it's the last two-thirds of December that [is projected].

CHAIRMAN VOLCKER. The last two-thirds of December is estimated. We only have a preliminary number for the 10th, so in that sense it's even more than that.

SPEAKER(?). It's three-quarters.

CHAIRMAN VOLCKER. Well, two-thirds. I stand to be corrected here, but I think I'm right that the current level for the 3rd and the estimated level for the 10th is a hair below the November average.

MR. AXILROD. Yes, in the case of M-1A, it's a hair below.

MR. BALLES. This is John Balles. I wonder if I could ask Steve a question. If you adjusted the original ranges for M-1A and B that we had, based on the 2-point spread that's developed instead of the 1/2 point you [previously] assumed, what would you say the revised ranges would be, Steve?

MR. AXILROD. Well, it depends a bit on what we assume came out of demand deposits and what we assume came out of other deposits. If we said it was 50/50, that would reduce the 3-1/2 to 6 percent M-1A range to something like 2-3/4 to 5-1/4 percent. I may be off a bit. And it would raise the 4 to 6-1/2 percent M-1B range to something like 4-3/4 to 7-1/4 percent. But don't hold me to precision on those numbers. That is the order of magnitude.

CHAIRMAN VOLCKER. Actually, that makes it appear in this estimate that we are within 1/4 percent or so of the--

MR. AXILROD. Well, I would have to--

CHAIRMAN VOLCKER. It is just that we are in the neighborhood of 1/2 point or so from the top of the range, if we don't get a big burst in the December data. We always have these ifs, but they can't change [unintelligible] unless we get another $9 billion item. I have been [surprised] by these figures too many times to say anything! Okay. Thank you very much.

END OF SESSION